

COMMONWEALTH OF MASSACHUSETTS
DEPARTMENT OF TELECOMMUNICATIONS AND ENERGY

-----X
Hearing Officer Notice Soliciting Comments on Whether the :
Department Should Open an Investigation to Establish an : Case: D.T.E. 03-45
Instate Universal Service Fund :
-----X

**REPLY COMMENTS OF
RICHMOND CONNECTIONS, INC. D/B/A RICHMOND NETWORKX
ON HEARING OFFICER NOTICE SOLICITING COMMENTS**

Dated: July 2, 2003

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I. INTRODUCTION

Comments have been filed in this matter by Richmond Connections, Inc. d/b/a Richmond NetWorx (“Richmond NetWorx” or the “Company”), Richmond Telephone Company (“Richmond Tel”),¹ AT&T Communications of New England, Inc. (“AT&T”), Verizon Massachusetts (“Verizon MA”), Verizon Wireless (“Verizon Wireless”), and PAETEC Communications, Inc. (“PAETEC”). According to the May 29, 2003 Hearing Officer Notice issued by Hearing Officer Chin (the “Hearing Officer Notice”), comments were to respond to two issues:

1. Whether the Department has sufficient statutory authority under existing federal and state statutes to establish a USF for the Commonwealth; and, if so,
2. Whether the Department should initiate an investigation into the establishment of a USF for the Commonwealth.²

Richmond NetWorx hereby replies to those comments. As shown below, those comments, taken as a whole, serve to respond in the affirmative to the two questions posed in the

¹ Richmond NetWorx and Richmond Tel are affiliates. Richmond NetWorx is a Competitive Local Exchange Carrier (“CLEC”) and Richmond Tel is an Incumbent Local Exchange Carrier (“ILEC”).

² Several commenters, most notably Verizon MA, went well beyond the scope of the Hearing Officer’s delineation of issues offering the conclusion, unburdened by any record support, that no instate USF system is required.

Hearing Officer Notice. In the interest of brevity, the comments of each party are summarized in the attachments to this reply. Attachment 1 is a matrix summarizing the positions taken by the commenters on the first issue posed by the Hearing Officer Notice. Attachment 2 is a matrix summarizing the positions taken by the commenters on the second issue posed by the Hearing Officer Notice.

II. THE POLITICAL LANDSCAPE

Not surprisingly, there is a clash of positions on the question of whether the Department has the necessary authority under Massachusetts law to establish an instate USF and whether it should institute an investigation to determine if such an instate USF should be created. The different positions are politically driven, in that the group of commenters that support an investigation are those whose business operations are hindered by the existing scheme of implicit subsidization of residential rates. By use of the phrase “the existing scheme of implicit subsidization of residential rates,” Richmond NetWorx is describing the present, policy-driven system of fostering above cost non-residential rates to preserve residential rates at levels that in some, if not most, areas, do not recover service costs. This group of supporters is represented by the following commenters: Richmond NetWorx, AT&T and Richmond Tel. For purposes of categorization, this first group will be collectively called the “USF Investigation Supporters.” The second group of commenters – Verizon MA and Verizon Wireless – are, for different reasons, happy with the status quo, antiquated system of implicit subsidization of residential

rates.³ For purposes of categorization, the two Verizon companies will be collectively called the “USF Investigation Opponents.”

The USF Investigation Supporters take their positions for two fundamental reasons:

- (i) the current regime of implicit subsidization harms interexchange carriers because intrastate access charges are maintained at rates substantially above cost and above interstate levels. The artificially high level of intrastate access charges also harms rural ILECs because it fosters uneconomic bypass; and
- (ii) the current requirement that Verizon MA maintain averaged residential rates and deaveraged UNE loop rates, forcing retail rate levels, at least in rural areas, to be lower than those of component UNE loops, hinders CLEC competition for residential service.

An instate USF system would help ameliorate these problems by making universal support for residential services competitively neutral, while driving non-residential and intrastate access rates toward incremental costs.

The USF Investigation Opponents take their positions because they are favored by the present universal service funding scheme, which features implicit subsidization of residential services by above-cost pricing of non-residential services. Verizon MA, serving as it does almost the entirety of the urbanized, lower cost areas of the Commonwealth, has the opportunity to “average away” the high costs of rural residential service and to maintain averaged residential rates. Understandably, it has no real incentive to encourage the kind of instate USF system that might foster competition for non-urban residential customers.⁴ Verizon Wireless, as a potentially

³ PAETEC is a special case in that it opposes any subsidization as a matter of principle, but, laudably, is willing to have the instate USF issue explored in a new proceeding. PAETEC misstates in their comments that Richmond Connections is an ILEC with 1,200 access lines when in fact Richmond Connections is a CLEC with over 3,000 access lines.

⁴ Little credibility should be given the Verizon MA argument that CLECs can compete in a meaningful way for rural residential customers by obtaining UNEs, even though those UNEs are priced higher than retail rates for residential service, or resale arrangements. Inherent in this argument is the proposition that a carrier offering an array of services to a customer can make a profit even if one of the underlying services is priced below its costs. Verizon MA may be able to benefit under this logic because its broad geographic

substantial payor into an intrastate USF, does not care to make such payments, notwithstanding the obvious value it receives from a ubiquitous wireline network.

The political motivations of each group of parties is an obvious driver of the positions taken by the “members” of each group on whether the Department has the authority to investigate creation of an intrastate USF. It is not surprising, then, that the USF Investigation Supporters find that the broad sweep of statutory powers granted the Department to regulate the telecommunications industry carries with it the implied power, already being exercised, in universal service funding matters. Similarly, the motivations of the USF Investigation Opponents suggest why they take the very cramped and rigidly formalistic view that the Department lacks express statutory power to create an intrastate USF, barring investigation of the need for such a scheme.

III. THE DEPARTMENT HAS THE NECESSARY STATUTORY POWERS

To the extent that the commenters are in agreement on any point, that agreement is on the question of whether the Commonwealth is allowed, under Section 254 of the Communications Act of 1934, as amended, 47 U.S.C. §254 to investigate an intrastate USF.⁵ The agreement is that the Commonwealth is so allowed.

No such agreement is to be had on the question of Commonwealth authority to conduct investigation of an intrastate USF. AT&T’s comments concisely summarize the position of the USF Investigation Supporters: (i) the D.T.E. has the necessary power under its plenary

footprint and complement of services, including interLATA long distance, allow an averaging of costs that, on the whole, is unavailable to any competitor today. Suffice it to say that, without rate rebalancing or an intrastate USF, a larger share of a dollar’s worth of long distance revenue from a Verizon residential customer in rural Massachusetts “falls to the bottom line” than would be the case with a dollar’s worth of long distance revenue from a Richmond NetWorx customer in the same area.

⁵ Verizon Wireless was silent on the question.

authority to regulate carrier rates and services, judicially acknowledged by the deference given by the courts to agency expertise in areas where the Legislature has granted it authority (AT&T, pp. 5-6); and (ii) the D.T.E. has long been involved in universal service by its history of favoring ILEC rates for non-residential services above cost in order to provide universal services at affordable rates (AT&T, p. 8).

The cramped, formalistic position of the USF Investigation Opponents is characterized by the contention that, if the Legislature intended that the D.T.E. have the power to create an instate USF, a system characterized by assessments upon carriers and distributions to a subset of carriers, it would have specifically done so in a precisely tailored statute as it has done in other areas. This position ignores the facts that (i) the Department has long fostered a universal service funding system of indirect or implicit subsidization by which ILEC rates for interexchange access services, for example, recover more than their costs in order to allow those ILECs to maintain “affordable” rates for residential services; and (ii) the Department has exercised powers implied from its general authority over rates in many areas, not the least of which were the rate restructuring and rebalancing proceedings described by Verizon MA at page 7 of its comments, as follows, “. . . D.T.E. 01-20 (TELRIC Proceeding) and D.T.E. 01-31 (Alternative Regulation Proceeding). The effect of those rate changes was to deaverage and reduce wholesale UNE rates and to increase retail rates on a statewide, averaged basis, respectively. . .” As the Department noted in the D.T.E. 01-31 Phase II Order, at 6,

While the General Court [(i.e., the Commonwealth’s body of statutory law)] specifies that rates are to be ‘just and reasonable’ and that rates should provide a utility with ‘reasonable compensation’ with reference to the service provided, neither of these two statutes [G.L. 159 §§ 14 and 20] prescribe a particular method by which the Department must fulfill its statutory mandate of ensuring just and reasonable rates or limit the Department to a specific regulatory scheme, such as cost-of-service, rate of return ratemaking, or regulation through a price cap [citations omitted].

Simply put, the Department has long been recognized to hold powers reasonably implied from its general regulatory and rate jurisdiction. Further, it has long exercised jurisdiction, under its power to ensure just and reasonable rates, over universal service funding by fostering the implicit subsidization system that the USF Investigation Supporters hope to convert to an explicit, competitively neutral and pro-competitive instate USF system. There is no merit to the contention that the Department lacks the jurisdictional power to do so.

IV. THE D.T.E. SHOULD INITIATE AN INVESTIGATION INTO AN INSTATE USF

The positions and arguments of each side on this issue are already summarized in this reply. Those positions and arguments require little more comment.

Much of what Verizon MA asserts in its comments requires a response. This is so because those comments, in large measure, go well beyond the scope of the relevant issue of whether the Department should investigate an instate USF to suggest that no need exists to establish a USF. The irrelevance of Verizon MA going beyond the scope of the issue posed aside, what is interesting is that so many of its assertions in support of its arguments against creation of an instate USF are so misleading and/or unsupported. These assertions actually help to demonstrate something that is just the opposite of what Verizon MA intended – that an investigation into an instate USF is needed. Examples of these assertions are:

(1) The claim that “[Richmond NetWorx] has provided no support of its claim that it cannot compete effectively with Verizon MA in Western Massachusetts . . . there are no ‘arbitrage opportunities or price squeeze problems . . . (Verizon MA, p. 2).” Richmond NetWorx believes, along with the Hearing Officer, as evidenced in the Hearing Officer Notice, that the purpose of an investigation is to garner evidence to see if further Department action is required. Without

there being any record evidence, including any to support its own assertions, Verizon MA damns even the idea of an investigation. Its pronouncement that there is no problem is a naked conclusion entitled to no credence. Infact, it is not surprising that Verizon does not see the need for an instate USF. Verizon currently has a significant pricing advantage in rural markets of Massachusetts and the creation of a USF would serve to even the playing field. An instate USF is essential to eliminate the pricing squeeze problems created by deaveraged wholesale rates and averaged retail rates.

Verizon is narrowly interpreting the principles of universal service to their benefit. Section 254(b) of the Telecommunications Act provides six specific principles on which the FCC and the Joint Board must base its policies for the preservation and advancement of universal service. Verizon would have us believe that only 254(b)(3), access in rural and high cost areas, should be reviewed in assessing the need for support⁶. While this is one guiding principle, 47 U.S.C. § 254(b)(2) also dictates that universal service support should be used to provide access to advanced telecommunications and information services for all regions of the Nation. By providing DSL in rural Massachusetts, NetWorx is offering rural customers a service that is not ubiquitous in the Verizon network. However, the high loop cost charged by Verizon works against CLECs such as NetWorx by eroding what thin margin might exist today. The creation of an instate USF would provide support for carriers that seek to bring advanced services to rural Massachusetts.

Verizon's deaveraged retail pricing effectively stifles competition in rural markets.

Local loops serving rural areas are more expensive than their urban counterparts. The Verizon pricing of unbundled local loops in the rural areas of Massachusetts proves this point. While an

⁶ Verizon Comments at Page 6.

urban loop can be purchased for \$10.90 per month, a rural loop costs \$24.40. In fact, the rural rate is nearly 75% higher than the statewide average rate for Verizon loops of \$13.99. The deaveraged pricing of local loops, combined with statewide average retail rates creates a price squeeze that works to the benefit of Verizon in rural markets. Verizon attempts to mask this point by drawing in any and all revenues from the variety of services offered by NetWorx⁷. While NetWorx certainly agrees there are sources of revenue in addition to local service, not all customers will elect to purchase the entire suite of services offered by the Company. In other words, other services will contribute revenues which will help to offset the cost of the local loop. This treats the local loop as a joint and common cost, one that is recovered through charges assessed on a variety of services. This is an interesting assertion which seems completely contradictory to Verizon's position in D.T.E. 01-31-Phase II. In that proceeding Verizon contended that the local loop is not a joint and common cost. The fact that various providers of usage services rely on the local loop to deliver their services to the end-user may lead some observers to arrive at the conclusion that the loop is a shared facility. The local loop is actually an output service that is "demanded in its own right" and must be identified with the full cost that is added to the network when a local loop is placed in service (Exh. VZ-6 at 7). In the D.T.E. Order in 01-31-Phase II, a comparison was made between the local service revenue for One Party Unlimited Local Residential Service ("1FR") and the cost of unbundled elements a competitor would be required to purchase to provide this same service⁸. This assessment showed retail rate of \$25.30⁹ for the service, and a cost to Verizon's competitors of \$23.72 per line per

⁷ Verizon Comments at Page 8.

⁸ D.T.E. 01-31-Phase II Order at Pages 81-82.

⁹ This current rate for Verizon's 1FR service is calculated as follows: \$12.36 (dial-tone line charge) + \$6.00 (Federal subscriber line charge) + \$6.94 (unlimited local usage). See Tariff M.D.T.E. No. 10, Part M, Section 1, Page 14, and also Tariff F.C.C. No. 11, Page 31-3.

month. Based on the Verizon June 9, 2003 compliance filing, changes are necessary to determine the cost incurred by Verizon competitors. First, and most importantly, the local loop cost used in the Order of \$15.26¹⁰ should be replaced by the rural loop rate. Also, port and switching charges should be revised to show the rates from the June 9th compliance filing. When these changes are made, the retail rate of \$25.30 pales in comparison to the \$34.87¹¹ a competitor would have to pay for the same network elements. The wholesale cost to a competitor is nearly 40% higher than the retail fees charged to an end user. While NetWorx agrees that bundling of services can sometimes help to overcome a lack of profitability in dial tone line charges, it is extremely difficult to find a package of services that contributes the \$9.58 per line per month of EBITDA (Earning Before Interest Taxes Depreciation and Amortization) required just to break even on this sale. The D.T.E. in the 01-31-Phase II Order indicated that it may, in a future docket, consider adoption of a universal service funding mechanism to reduce the arbitrage opportunities and the price squeeze problems presented by the interaction of deaveraged wholesale prices and averaged retail prices¹². Based on the analysis above, now is the time to undertake such a review for the sake of advancing all universal service principles for rural Massachusetts.

(2) The claim at page 7 of the Verizon comments that Richmond NetWorx is really seeking, “. . . a further reduction in UNE rural loop rates – under the ruse of an instate USF” is, to characterize it charitably, misleading. If Richmond NetWorx is attacking anything obliquely, it is the current Department requirement and Verizon MA practice of maintaining

¹⁰ D.T.E. 01-31-Phase II Order at Page 82, Footnote 67.

¹¹ This cost is calculated using a 24.99 percent retail markup and the following UNE rates: \$24.40 (rural loop) + \$2.57 (port) + \$0.9294 (switching [assuming a typical 600 minutes of use per month]) (1.2499) = \$34.87.

¹² D.T.E. 01-31-Phase II Order at Page 83.

deaveraged UNE loop rates and averaged residential rates. The Company is not attacking the deaveraged UNE loop rates or current requirement for averaged residential rates, *per se*. What it is asserting is that, if the requirement for averaged residential rates is to continue, then an in-state USF must be created to allow competition for residential customers in rural areas. Verizon MA's position is understandable, if untenable – it does not care to see a system created that increases competition in rural areas.

(3) The claim, at page 8 of the Verizon MA comments, that the opportunity to resell Verizon's services is a panacea for any problems that Richmond NetWorx might experience in competitive entry is disingenuous, at best. It is certainly ungenerous in that it offers Richmond NetWorx the barest opportunity to control its own destiny in a competitive market. First, as clearly stated in its comments, Richmond NetWorx is a facilities-based CLEC and intends to remain primarily a facilities-based CLEC. The reason for this is obvious – its long-term competitive survival is possible only by avoiding dependence upon Verizon MA's resold offerings. The Richmond NetWorx business model is the kind of competitive threat feared most by Verizon MA – a facilities-based competitor with its own switch, dependent upon Verizon MA only for "last mile" access.

Based upon the foregoing examples of unsupported positions asserted by Verizon MA, as irrelevant as they may be to the question of whether the Department should investigate an in-state USF, it is clear why Verizon MA wants to avoid such an investigation. In fact, Verizon MA's efforts demonstrate exactly why such an investigation should be conducted.

V. CONCLUSION

It is clear that the Department has the necessary authority to investigate an instate USF and that the need exists to do so. Accordingly, Richmond NetWorx urges that such an investigation be commenced as quickly as practicable.

Respectfully submitted,

Christa M. Proper
Vice President
Richmond Connections, Inc.
d/b/a Richmond NetWorx

July 2, 2003

**DOES THE DEPARTMENT HAVE SUFFICIENT AUTHORITY UNDER
EXISTING FEDERAL AND STATE STATUTES TO ESTABLISH A USE
FOR THE COMMONWEALTH?**

**DOES THE DEPARTMENT HAVE SUFFICIENT AUTHORITY UNDER
EXISTING FEDERAL AND STATE STATUTES TO ESTABLISH A USF
FOR THE COMMONWEALTH?**

<u>Commenter</u>	<u>Yes/No?</u>	<u>Rationale For Position</u>
Richmond NetWorx	Fed – Y MA-- Y	- Communications Act Section 254(f) (p. 3). - MA statutes grant broad area of regulatory powers to D.T.E. and host of traditional specific powers (p. 6) - DTE has exerted its powers beyond those specifically delineated in statutes, such as methodology for regulatory schemes for rate regulation (p. 7). - DTE has already involved itself in universal service regulation in absence of express statutory authority by Phase II Order's requirement of deaveraged UNE rates, but averaged residential rates (p. 8).
Richmond Telephone	Fed – Y MA -- Y	- Explicit in federal law (p. 2). - D.T.E. has broad, general regulatory authority and introduction of a Commonwealth USF would be an extension of existing rates (pp. 2-3).
AT&T	Fed – Y MA -- Y	- Explicit in Communications Act Section 254 (p. 3). - D.T.E. has necessary power under its plenary authority to regulate carrier rates and services, judicially acknowledged by deference given to agency expertise in areas where Legislature has granted it authority (pp. 5-6). - D.T.E. has a long history of maintaining some ILEC rates above cost in order to provide universal services at affordable rates (p. 8).
Verizon MA	Fed-- Y MA -- N	-Allowed under Communications Act 254, but is not an independent source of authority for state to establish a USF (p. 3). -No explicit authority to assess fees or create a special fund for USF given to D.T.E. by statute, unlike other statutes in which such authority for fee assessment or creation of special funds was created (p. 4). Funding mechanism creation allowable only when specific authorization is given by statute; cannot be implied from general statutory power (p. 5).
Verizon Wireless	Fed— MA --N	- No statutory authority authorizing DTE to require contributions from carriers or customers to subsidize other carriers or customers (p.3). - No statutory power over rates and service of CMRS carriers (p. 4). - Only mention of universal service in statutes is for gas and electric, not telecom (p. 4).
Paetec	Fed – Y MA - Y	- Explicit in Federal law (p.2). - Clear and compelling, if not explicit (p.2).

**SHOULD THE DTE OPEN AN INVESTIGATION INTO
ESTABLISHMENT OF A COMMONWEALTH USE?**

SHOULD THE DTE OPEN AN INVESTIGATION INTO ESTABLISHMENT OF A COMMONWEALTH USF?

<u>Commenter</u>	<u>Yes/No?</u>	<u>Rationale For Position</u>
Richmond NetWorx	Yes	-Price squeeze inherent in Verizon's maintenance of deaveraged UNE loop prices and averaged residential rates in Western MA precludes entry into residential competition in rural western Massachusetts area served by this CLEC (p. 2), a fact implicitly acknowledged by DTE in D.T.E. 01-31-Phase II Order at p. 83 (p. 3).
Richmond Telephone Company	Yes	-Remaining implicit support inherent in intrastate rates and resultant, artificially high intrastate access rates, due to lack of Commonwealth programs to move to explicit support, has led to loss of ILEC access revenues (p. 4). -An instate USF would ameliorate need for small, rural ILECs to recover lost revenue without need to increase local rates beyond affordability level (p. 4). -An in-state USF would eliminate access customer "forum shopping" incentive inherent in present disparity between inter- and intrastate access rate levels (p. 4-5).
AT&T Communications	Yes	"[A]bove cost access charges [of ILECs, due to the lack of ability to raise below cost residential rates or access to a Commonwealth USF] are inherently anticompetitive . . . Above cost access pricing ultimately threatens the viability of the wireline network, because it drives consumers to by-pass . . . the traditional wireline network to make toll calls, using for example wireless and voice over IP ('VOIP') technologies. The result undermines the traditional wireline network and potentially creates uneconomic bypass, inadvertently subsidizing alternative technologies that may not be competitive in their own right. Above cost access worked only as long as consumers had no way to by-pass it. Now that they do, another means of financing universal service requirements is needed" (p. 12).
Verizon MA	No	- No showing of services available in nonrural areas that are not available in rural areas or, if available, are priced higher than in nonrural areas (p. 6). - No showing of price squeeze between Verizon MA wholesale rates in western MA and its retail rates. Decisions in D.T.E. 01-20 and 01-31 deaveraged and reduced UNE rates and increased retail rates on a statewide, averaged basis. Richmond NetWorx merely seeking a "further rate reduction in UNE rural loop rates – under ruse of an instate USF" (p. 7). - No showing that Verizon MA's rural UNE loop rates are higher than its retail rates; even if it was true, Richmond NetWorx could compete by reselling Verizon's services (pp. 8-9).
Verizon Wireless	No	- Richmond NetWorx has failed to show any need for a Commonwealth USF (p. 7) - Richmond NetWorx looking for subsidization by other carriers in order to lower its prices (p. 7)
Paetec	No	- Belief that Richmond NetWorx is seeking USF to bolster weakening balance sheet rather than seeking to enhance public interest. Competition is what the market needs (p. 4).